

## U.S. Securities and Exchange Commission Provides Guidance on Climate Change Disclosure

On February 2, 2010, the U.S. Securities and Exchange Commission issued Release Nos. 33-9106; 34-61469, titled “Commission Guidance Regarding Disclosure Related to Climate Change.” (the “Release”), available at <http://www.sec.gov/rules/interp/2010/33-9106.pdf>. Because this interpretive release becomes effective upon publication in the *Federal Register*, the SEC’s guidance on climate change disclosure is applicable to upcoming annual reports on Form 10-K, as well as other SEC filings, such as registration statements, quarterly reports and reports filed by most foreign private issuers.

The Release does not implement any new disclosure rules or modify any rules currently in effect. Rather, it describes how the SEC believes its current regulations apply to the issues raised by climate change.

### Existing Disclosure Requirements Applicable to Climate Change

The Release describes existing Regulation S-K items that may require climate change disclosure in appropriate circumstances. For example, Item 101, the description of business section, expressly calls for disclosure of the material effects that compliance with enacted federal, state and local environmental provisions may have upon the capital expenditures, earnings and competitive position. Similarly, Item 103, the legal proceedings item, contains specific disclosure requirements for certain material environmental litigation. Item 503(c) of Regulation S-K mandates disclosure of risk factors. Item 303, management’s discussion and analysis (MD&A), requires disclosures of known trends, events, demands, commitments and uncertainties that are reasonably likely to have a material effect on financial condition and operating performance. There are parallels to these disclosure requirements that are applicable to most foreign private issuers.

### Ways in Which Climate Change May Trigger Disclosure

The SEC identified four topics to illustrate how climate change may trigger disclosure obligations under current SEC rules.

**Impact of Legislation and Regulation.** The Release notes that there have been significant developments in federal and state legislation and regulation regarding climate change. To the extent that such legislation deals with greenhouse gas (GHG) emissions, Item 101 requires disclosure of capital expenditures for environmental control facilities. The Release advises companies to consider how legislation and regulation may specifically affect them when preparing risk factor disclosure, noting that companies in the energy sector may face significantly different risks from climate change legislation or regulation than companies that currently rely on products that emit greenhouse gases, such as those in the transportation sector.

When drafting the MD&A, companies should assess whether any climate change legislation or regulation that has been adopted is reasonably likely to have a material effect on their financial condition or results of operation. Pending legislation or regulation should be analyzed as a known uncertainty, meaning that management must evaluate whether such legislation or regulation is reasonably likely to be enacted. Unless management determines that it is not reasonably likely to be enacted, the Release specifies that companies must proceed on the assumption that the legislation or regulation *will* be adopted.

Next, management must determine whether the proposed legislation or regulation, if enacted, is reasonably likely to have a material effect on the company, its financial condition or results

of operation. Unless such a material effect is not reasonably likely, the MD&A would have to disclose the potential effect of such pending legislation or regulation.

If material, the MD&A may disclose the difficulties in assessing the timing or effect of such pending legislation or regulation. The Release notes that it is appropriate to consider new opportunities arising from pending legislation and regulation, as well as negative consequences.

The Release provides the following examples of possible consequences arising from pending climate change legislation or regulation:

- Costs to buy GHG allowances or “offsets” under a “cap and trade” system, as well as profits from their sale;
- Costs required to improve facilities and equipment to reduce emissions; and
- Changes in profits or losses arising from increased or decreased demand for goods and services, whether arising directly from such legislation or regulation or indirectly from changes in costs of goods sold.

**International Accords.** The Release also advises companies to disclose, if material, the impact of treaties or international accords relating to climate change. The potential sources of disclosure obligations are the same as are applicable to U.S. climate change legislation and regulation.

**Indirect Consequences of Regulation or Business Trends.** Various developments relating to climate change may create new opportunities and risks that may have indirect consequences for companies. For example, the Release suggests considering whether the following should be disclosed as a risk factor, in the MD&A or, in certain circumstances, in the business description:

- Decreased demand for goods that produce significant GHG emissions;
- Increased demand for goods that result in lower emissions than competing products;
- Increased competition to develop innovative new products;
- Increased demand for generation and transmission of energy from alternative energy sources;

- Decreased demand for services related to carbon based energy sources, such as drilling services or equipment maintenance services; and
- Reputational damage from the public’s perception of any publicly available data relating to GHG emissions that potentially could harm a company’s business operations or financial condition.

**Physical Impact of Climate Change.** The Release specifies that companies that are vulnerable to severe weather should consider disclosing the material risks and consequences of such events in their public filings. It identifies the following possible consequences of severe weather:

- Property damage and disruptions to operations, either to manufacturing operations or the transportation of products (for companies with operations concentrated on coastlines);
- Indirect financial and operational impacts from severe weather disruptions to the operations of major customers or suppliers;
- Increased insurance claims and liabilities (for insurance and reinsurance companies);
- Decreased agricultural production capacity; and
- Increased insurance premiums and deductibles, or a decrease in the availability of coverage (for companies in areas subject to severe weather).

## Practical Considerations

Because the climate change guidance applies to existing rules, public companies need to immediately assess whether they should add or expand climate change disclosure in their future SEC filings. Timing is particularly crucial for calendar year-end companies that are in the process of preparing their annual reports on Form 10-K.

It is important to monitor pending climate change laws and regulations, as well as international accords, in order to determine disclosure obligations. Companies may want to develop a disclosure control or procedure to address this concern.

Companies need to evaluate the extent to which they are affected by the impact of climate change on other entities with whom they have dealings. This is another area in which a disclosure control or procedure may be appropriate.

Because of the SEC's interpretation that reputational damage related to climate change may need to be disclosed, it may be appropriate for some companies to consider including public relations personnel in the disclosure control process.

The SEC has indicated that it will monitor the impact of the Release on public filings as part of its ongoing disclosure review program. Therefore, public companies should be aware that they might receive comments on climate change disclosure from SEC staff.

The SEC's interpretive guidance may not be its last statement on climate change issues. The SEC's Investor Advisory Committee is considering climate change disclosure as part of its mandate to provide recommendations to the SEC. In addition, the SEC is

planning to hold a public roundtable on disclosure regarding climate change matters this spring. Based on this input and its review program, the SEC will determine whether further guidance or rulemaking relating to climate change disclosure is appropriate. ♦

*If you have any questions about the SEC's climate change disclosure interpretations, or any other matter raised in this Update, please contact the author, or any of the partners in our [Corporate & Securities practice](#), our [Climate Change practice](#), or our [Environmental practice](#).*

**Laura D. Richman**

+1 312 701 7304

[lrichman@mayerbrown.com](mailto:lrichman@mayerbrown.com)

---

Mayer Brown is a leading global law firm with more than 1,750 lawyers worldwide, including approximately 1,000 in the Americas, 450 in Europe and 300 in Asia. We serve many of the world's largest companies, including a significant proportion of the Fortune 100, FTSE 100, DAX and Hang Seng Index companies and more than half of the world's largest investment banks. We provide legal services in areas such as Supreme Court and appellate litigation; corporate and securities; finance; real estate; tax; intellectual property; government and global trade; restructuring, bankruptcy and insolvency; and environmental.

OFFICE LOCATIONS AMERICAS: Charlotte, Chicago, Houston, Los Angeles, New York, Palo Alto, Rio de Janeiro, São Paulo, Washington  
ASIA: Bangkok, Beijing, Guangzhou, Hanoi, Ho Chi Minh City, Hong Kong, Shanghai  
EUROPE: Berlin, Brussels, Cologne, Frankfurt, London, Paris

ALLIANCE LAW FIRMS Mexico (Jáuregui, Navarrete y Nader); Spain (Ramón & Cajal); Italy and Eastern Europe (Tonucci & Partners)  
Please visit our web site for comprehensive contact information for all Mayer Brown offices.  
[www.mayerbrown.com](http://www.mayerbrown.com)

This Mayer Brown publication provides information and comments on legal issues and developments of interest to our clients and friends. The foregoing is not a comprehensive treatment of the subject matter covered and is not intended to provide legal advice. Readers should seek specific legal advice before taking any action with respect to the matters discussed herein.

IRS CIRCULAR 230 NOTICE. Any advice expressed herein as to tax matters was neither written nor intended by Mayer Brown LLP to be used and cannot be used by any taxpayer for the purpose of avoiding tax penalties that may be imposed under US tax law. If any person uses or refers to any such tax advice in promoting, marketing or recommending a partnership or other entity, investment plan or arrangement to any taxpayer, then (i) the advice was written to support the promotion or marketing (by a person other than Mayer Brown LLP) of that transaction or matter, and (ii) such taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor.

© 2010. Mayer Brown LLP, Mayer Brown International LLP, and/or JSM. All rights reserved.

Mayer Brown is a global legal services organization comprising legal practices that are separate entities (the Mayer Brown Practices). The Mayer Brown Practices are: Mayer Brown LLP, a limited liability partnership established in the United States; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales; JSM, a Hong Kong partnership, and its associated entities in Asia. The Mayer Brown Practices are known as Mayer Brown JSM in Asia. In Brazil Mayer Brown is in association with Tauil & Chequer Advogados, a Brazilian law partnership. "Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.